March 13, 2006

Board of Commissioners
Department of Telecommunications & Energy
Judith F. Judson, Chairman
One South Station
Boston, Massachusetts 02110

RE: Request for Advisory Opinion on Fiscal Controls for Municipal Utilities

Dear Board of Commissioners and Chairman Judson:

This office is requesting that the Department of Telecommunications and Energy ("DTE") issue an advisory opinion specific to municipal light department reporting requirements in order to prevent and discourage the types of unsound business practices described in this Office's December 2005 report, *An Investigation of the Use of Certain Bond Funds by the North Attleborough Electric Department* ("*Bond Funds Report"*).

Specifically, this Office respectfully requests that the DTE, for the reasons set forth below, issue an advisory opinion applicable to all public utility companies under the DTE's jurisdiction, which shall state as follows:

*Any Corporation subject to M.G.L. c.164, §3 shall cooperate with the municipal auditor, accountant, or treasurer of the city or town in which that Corporation is located and,*



*specifically, shall provide to that auditor, accountant, or treasurer all documentation requested by that auditor, accountant, or treasurer in the discharge of his or her*

*responsibilities under M.G.L. c.164, §56. The auditor, accountant, or treasurer shall not be required to provide any justification for any request, except that it is made pursuant to M.G.L. c.164, §56.*

DISCUSSION:

As noted in my letter dated December 29, 2005, the *Bond Funds Report* concludes that the North Attleborough Electric Department (NAED) management misspent $4.0 million in bond funds on an unauthorized internet venture that will cost the North Attleborough rate payers approximately $8.1 million. It is my belief that this situation could have been avoided had there been adequate fiscal controls to assure the propriety of the NAED's expenditures.

In the case of North Attleborough, proceeds from the sale of municipal bonds approved by the Town Meeting--based on the NAED's representations that funds were needed for certain NAED capital improvement projects--were used by the NAED management to invest in an unrelated internet venture. Our investigation disclosed that the NAED not only failed to disclose its intended use of bond funds to town officials, but that it did so contrary to advice of its own legal counsel, which advised the NAED in 1996 that bond funds can only be used for the purposes set forth in the authorization. *Bond Funds Report*, pp. 7-8.

It is our opinion that improper expenditures such as those made in connection with the internet venture would have been avoided had the NAED's fiscal operations been subject to a reasonable level of accountability. This situation was exacerbated by what we found to be "a corporate culture fostered by NAED management that resisted appropriate oversight by other Town bodies." *Bond Funds Report*, p. 15.

This office has identified similar problems in the municipalities of Braintree, Reading, Marblehead, Chicopee, and Littleton.

The relationship between a municipality and its gas or electric company with respect to administration of finances is set forth in M.G.L. c. 164, §56. Section 56 makes it clear that the manager of a municipal lighting plant is subject to the "direction and control" of the municipality. The statute provides that all monies paid to the gas or electric company shall be paid *to* the municipal treasurer, and that all accounts rendered to the gas or electric company shall be paid *by* the municipal treasurer. Payment requests

made on behalf of the gas or electric company are subject to municipal review:

> All accounts rendered to or kept in the gas or electric plant of any city shall be subject to the inspection of the city auditor or officer having similar duties, and in towns they shall be subject to the inspection of the selectmen. … The auditor or officer having similar duties in cities, and the selectmen in towns, shall approve the payment of all bills or payrolls of such plants before they are paid by the treasurer, *and may disallow and refuse to approve for payment, in whole or in part, any claim as fraudulent, unlawful or excessive*; and in that case the auditor or officer having similar duties, or the selectmen, shall file with the city or town treasurer a written statement of the reasons for the refusal; and the treasurer shall not pay any claim or bill so disallowed.

M.G.L. c. 164, §56 (emphasis added).

The issue raised by the statutory language is what records a municipal auditor needs in order to discharge his or her obligations under M.G.L. c.164, §56.

The statute authorizes an auditor to decline to pay an account rendered if the auditor has a reasonable belief that it is "fraudulent, unlawful, or excessive." Section 56 also states that its terms do not abridge the powers of town accountants under M.G.L. c.41, §§55-61. Section 55 states that a town accountant has the powers conferred on auditors under M.G.L. c.41, §§50-53. Those powers include the right to examine the books and accounts of all town officers and committees authorized with the receipt, custody or expenditure of money. The manager of a municipal light board is a town officer. *Commonwealth v. Oliver*, 342 Mass. 82, 84 (1961) (municipal light company). Moreover, the auditor shall have "free access to such books, accounts, bills and vouchers as often as once a month for the purpose of examination." M.G.L. c.41, §50.

In order to ascertain whether an account or bill is "fraudulent, unlawful, or excessive," an auditor must have access to related financial records. There is a belief among municipal gas and electric companies, however, that a municipality cannot ask for such records under Massachusetts decisional law. This results in an ineffectual process whereby an auditor can only disallow an account if it is fraudulent, unlawful, or excessive *on its*

*face*—a determination that is not ordinarily possible to make without back up documentation.

As far as this office can tell, the basis for this rule is a decision rendered by Superior Court Justice Herbert F. Travers, Jr. on December 18, 1996. In an unpublished decision, *Town of West Boylston v. Scirpoli* (Worcester Sup. Ct. Nos. 95-2154B & 95-2424B, Dec. 18, 1996), a municipality refused to pay certain invoices without supporting documentation. Justice Travers, citing *Municipal Light Comm'n of Peabody v.City of Peabody*, 348 Mass. 266 (1964), stated that the

> Supreme Judicial Court has made it clear that the management board [of an electric light Plant] is only required to conform with the accounting procedures used by the [DTE] and not any other requested by a town. …The Plant need not follow and procedures requested by the Town and/or its accountant which are inconsistent with those of the [DTE]. Thus, if the [DTE] does not require supplemental documentation to accompany invoices in their accounting for light bills, then the Town may no do so either.

*Scirpoli*, p 12.

We believe that Justice Travers read the *Peabody* case in a way that is inconsistent with the statute, with resulting harm to municipal taxpayers. The opinion also creates confusion among municipal auditors and managers of municipal gas and electric companies as to their respective rights and obligations.

In *Peabody*, the court was asked to issue a declaration of the powers and duties of the city with respect to annual appropriations for the municipal light department and of the city auditor with respect to the municipal light department's accounts and bills. With respect to appropriations, the court stated that the city was obliged to appropriate sufficient funds for annual plant expenses as determined by the plant manager. With respect to the payment of accounts and bills, the court stated that it could find no basis for

> the auditor's requiring a breakdown of the accounts of the light commission in accordance with the classifications operative in Peabody for the accounts of other city departments. The manager should, of course, furnish the auditor with a statement of the classifications under which he operates. See c. 164, §

> 63 [Records and reporting to the DTE]. He should make available to the auditor a copy of his budget. We assume that the manager would be cooperative in the event that the auditor should indicate certain nonburdensome adjustments in the detail of the commission's accounting or procedures that would facilitate the work of the auditor's office and which would be entirely consistent with the requirements of the Department.

*Peabody*, 348 Mass. at 272-73. The court then held that the "accounting procedures of the light department are to be as prescribed by the [DTE], and the commission and its manager are not to be required to conform to other procedures." *Id*. at 273. (Under 220 C.M.R. §51.01, DTE's accounting procedures are those adopted by the Federal Energy Regulatory Commission (FERC), which are found at chapter 18 of the Code of Federal Regulations, Part 101 (Uniform System of Accounts). It is our understanding that the DTE has not prescribed any additional required accounting procedures.)

The *Peabody* case does not support the broad preemption of fiscal oversight authority articulated by Justice Travers in *Scirpoli*. Rather, the case supports cooperation between a municipality and its gas or electric company. It does not limit the oversight responsibility of the auditor in paying accounts and bills, or the auditor's obligation to withhold payment for expenditures that he or she believes are fraudulent, unlawful or excessive. *Peabody* only states that a municipality cannot require a gas or electric company to follow accounting practices used by the municipality.

If an auditor is required by statute to decide whether an account or bill is fraudulent, unlawful or excessive, it is entirely reasonable that he or she should have some basis on which to make the determination. That basis can only be those supplemental documents that are the basis of an informed decision. This is not a case, as in *Peabody*, where the gas or electric company is being asked to follow the municipality's procedures. Rather it is a matter of simple prudence mandated by the

language of the statute.

The opinion requested would assist auditors in discharging their statutory responsibilities and will reduce the risk of losses such as those incurred by the NAED, the Town of North Attleborough, and other municipalities in the commonwealth.

Respectfully submitted,

Gregory W. Sullivan
Inspector General

Enclosures:
1- M.G.L. c.164, §56
2 - *Town of West Boylston v. Scirpoli* (Worcester Sup. Ct. Nos. 95-2154B & 95-2424B, Dec. 18, 1996)
3 - *Municipal Light Comm'n of Peabody v. City of Peabody*, 348 Mass. 266 (1964)